

Economic Watch

U.S.

Monthly US Outlook

No Clear Signs of a Significant Boost in 1Q12

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Economic Analysis

U.S.

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- **Economic news has been mostly positive, although some recent indicators suggest slowing activity for 1Q12**
- **Growth in 2012 should exceed that of 2011, but risks remain tilted to the downside**

Economic activity has improved since the low point in mid-2011, yet recent indicators have been less-than-exciting. In fact, we expect that the pace of expansion is likely to slow for 1Q12. Growth in 4Q11 was the strongest of 2011, at 2.8% QoQ annualized, and this momentum should partially carry over into 2012. In particular, personal consumption expenditures should remain similar, with continued strength in durable goods. Although recent declines in consumer confidence levels suggest some hesitation moving forward, improvement in labor market conditions should balance concerns. While the crisis in Europe has not affected all aspects of domestic activity, we expect that the downward pressure on exports will persist.

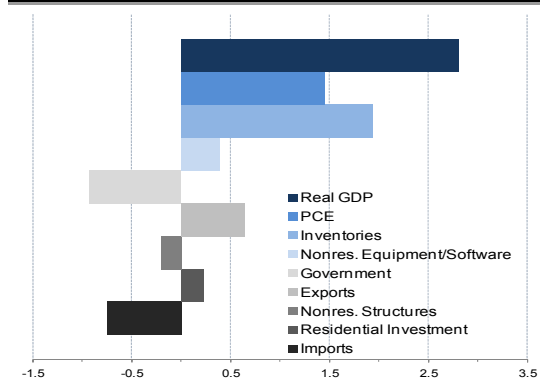
The lower-than-expected estimate for real GDP growth in 4Q11 is in line with Bernanke's view that the growth outlook is mixed and the recovery not "self-sustaining", prompting the Fed to revise down their growth projections for 2012 and 2013. We still regard the FOMC's projections of US GDP growth as too high, especially given the fiscal drag from expected future austerity measures in 2013. Bernanke regards the housing sector as partially responsible for the damaged link between monetary policy and economic activity. Therefore, any future scheme of large-scale asset purchases is likely to involve mortgage-backed securities. In its latest meeting, the Fed also released FOMC members' projections for the fed funds target rate for the first time, showing that the target fed funds rate will remain at or below 1% until the end of 2014. As implied by futures prices, the market had expected a first rate increase around 2014Q1 and the statement shifted expectations for interest rates considerably farther into the future. FOMC developments suggest that the probability of another round of large-scale asset purchases has increased but the Fed is not yet ready to embark on these purchases until either a tail risk event emerges or the data clearly suggests a significant slowdown in US growth. We expect that the Fed will be on hold until the beginning of 2014Q4. Moreover, Fed interventions and global uncertainties will keep long-term rates low, though we do expect a very moderate upward trend in yields.

The employment situation has been improving gradually but better than expected, with relatively stable growth in nonfarm payrolls and a decline in the unemployment rate to 8.3%. However, total nonfarm payroll levels have rebounded only 36% in the past two years compared to the pre-recession peak. Jobless claims data has been mostly positive, yet there has been no clear indication that business hiring plans will become less conservative in the near future. Even with January's boost in nonfarm payrolls, employment gains remain weaker than in 1Q11 but gives only some hope for the future of job growth.

Despite high rent costs and the recent bounce back in gas prices, we continue to expect that inflation will decelerate in the coming months, with core PCE inflation remaining within the Fed's comfort zone. Our growth outlook for 2012 is stronger compared to 2011, however, economic activity will be limited by downside risks, including slow job creation, housing stress, and continued global uncertainties. This economic environment and large economic slack should keep inflation under control. Furthermore, the rise in political uncertainty is likely to continue as the 2012 presidential campaign heats up. While risks remain tilted to the downside for 2012, another Lehman-type crisis is unlikely.

Economic Indicators

Graph 1
Contributions to Real GDP Growth
(4Q11 Advanced, SAAR % Points)



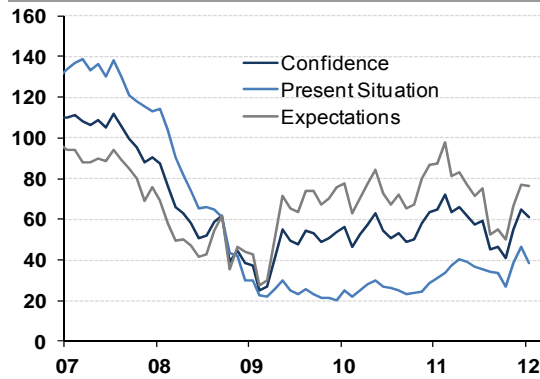
Source: Bureau of Economic Analysis

Graph 2
Personal Income and Expenditures
(3MMA, MoM%)



Source: Bureau of Economic Analysis

Graph 3
Consumer Confidence
(SA, Index 1985=100)



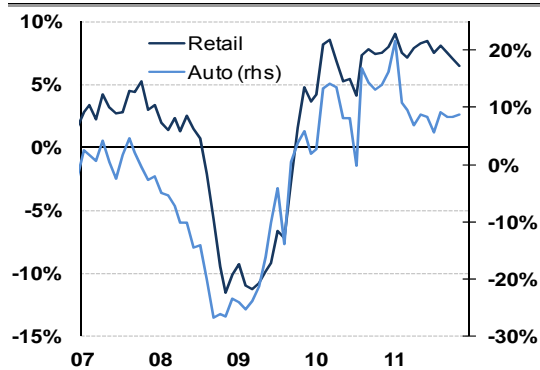
Source: Conference Board

Graph 4
ISM Indices
(SA, 50+ = Expansion)



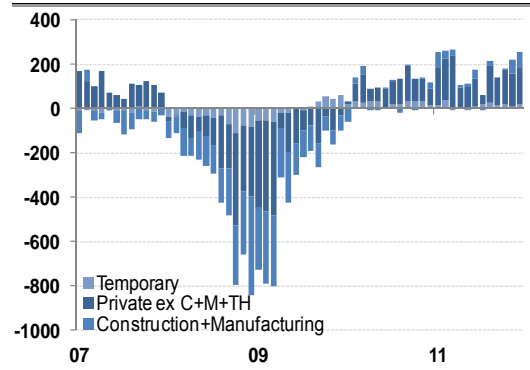
Source: ISM

Graph 5
Retail and Auto Sales
(YoY % Change)



Source: US Census Bureau

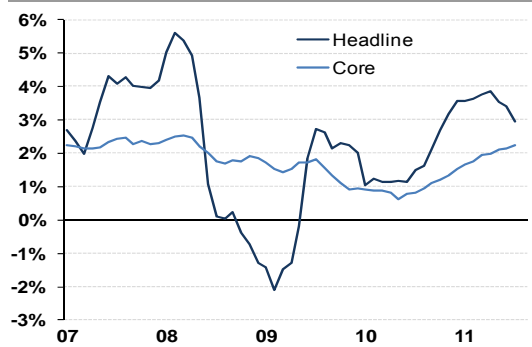
Graph 6
Private Nonfarm Payrolls
(Monthly Change in K)



Source: Haver Analytics & BBVA Research

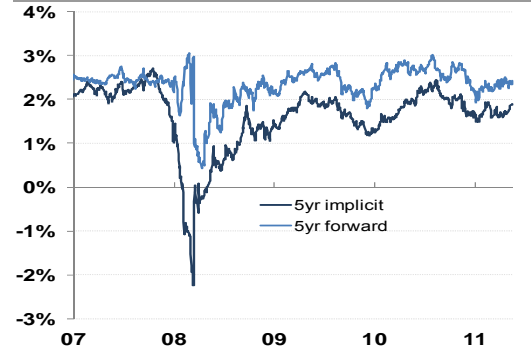
Economic Indicators

Graph 7
Consumer Price Index
(YOY% NSA, 1982-84=100)



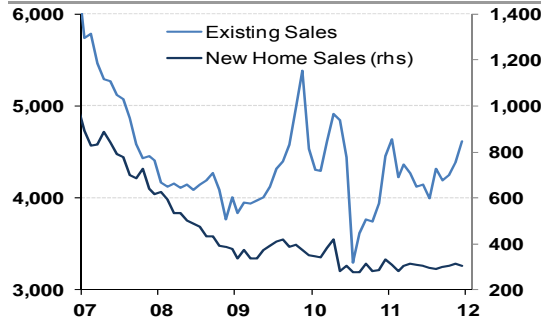
Source: Bureau of Labor Statistics

Graph 8
Inflation Expectations
(%)



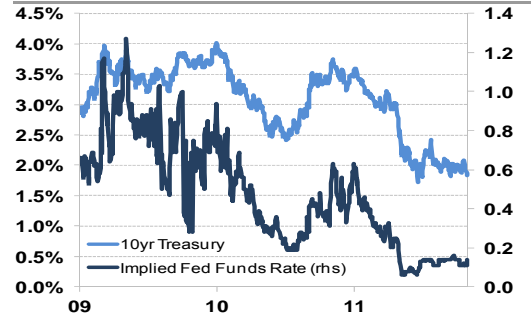
Source: Federal Reserve Board & BBVA Research

Graph 9
New and Existing Home Sales
(Thousands)



Source: Haver Analytics & BBVA Research

Graph 10
12 Month Implied Fed Funds Rate & 10 Yr Treasury
(%Yield)



Source: Haver Analytics

Table 1
Forecasts (BOLD=FORECASTS)

| | 2Q2011 | 3Q2011 | 4Q2011 | 2011 | 2012 | 2013 |
|-----------------------------------|--------|--------|--------|--------------|--------------|--------------|
| Real GDP (% SAAR) | | | | | | |
| GDP | 1.3 | 1.8 | 2.8 | 1.7 | 2.3 | 2.2 |
| Real GDP (Contribution, pp) | | | | | | |
| PCE | 0.7 | 1.7 | 2.0 | 1.5 | 1.6 | 1.5 |
| Gross Investment | 6.4 | 1.3 | 20.0 | 0.6 | 0.9 | 0.8 |
| Non Residential | 10.3 | 15.7 | 1.7 | 0.8 | 0.8 | 0.7 |
| Residential | 4.2 | 1.3 | 10.9 | 0.0 | 0.1 | 0.1 |
| Exports | 3.6 | 4.7 | 4.7 | 0.9 | 0.8 | 0.9 |
| Imports | 1.4 | 1.2 | 4.4 | -0.8 | -0.8 | -1.1 |
| Government | -0.9 | -0.1 | -4.6 | -0.5 | -0.1 | 0.1 |
| Unemployment rate (%) | 9.0 | 9.1 | 8.7 | 9.0 | 8.5 | 8.1 |
| Average Montly Nonfarm Payroll(k) | 130 | 128 | 157 | 137 | 158 | 176 |
| CPI | | | | | | |
| CPI (YoY%) | 3.4% | 3.8% | 3.3% | 3.2 | 2.3 | 2.3 |
| Core CPI (YoY%) | 1.5% | 1.9% | 2.2% | 1.7 | 1.9 | 1.8 |
| Fiscal balance (% GDP) | - | - | - | -8.5 | -7.1 | -4.6 |
| Current Account (bop, % GDP) | -3.3 | -2.9 | - | -3.2 | -3.2 | -3.4 |
| Fed target rate (% eop) | 0.25 | 0.25 | 0.25 | 0.25 | 0.25 | 0.25 |
| S&P Case & Shiller Index | 130.2 | 130.4 | - | 128.5 | 128.5 | 130.2 |
| 10Yr Treasury (% Yield, average) | 3.2 | 2.4 | 2.0 | 2.8 | 2.3 | 2.7 |
| US Dollar/ Euro | 1.44 | 1.41 | 1.35 | 1.31 | 1.27 | 1.26 |
| Oil Prices (dpb) | 117.6 | 113.3 | 109.5 | 113.5 | 99.0 | 102.5 |

Source: BBVA Research

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